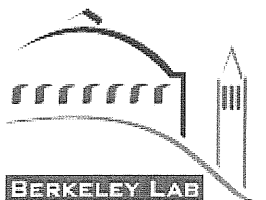


LAWRENCE BERKELEY NATIONAL LABORATORY
INTERNAL AUDIT SERVICES DEPARTMENT - DRAFT

ADVISORY SERVICES REPORT

OMB Circular A-123 Lessons Learned

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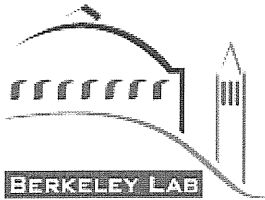
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MANAGEMENT SUMMARY

Background

In December 2004, the United States Office of Management and Budget released a revised Circular A-123, *Management's Responsibility for Internal Control*. The Circular was issued under the authority of the Federal Managers' Financial Integrity Act of 1982 and became effective fiscal year 2006. The revised Circular provides guidance to Federal managers on improving the accountability and effectiveness of Federal programs and operations by establishing, assessing, correcting, and reporting on internal control. The intent is to strengthen the process that management uses to assess internal control over financial reporting, specifically documentation, monitoring, and testing requirements. OMB Circular A-123 is similar to management compliance requirements for private corporations under the Sarbanes-Oxley Act, which was enacted in the wake of corporate fraud scandals.

In January 2005, LBNL management assembled a cross-functional team led by the Controller and included representatives from the Office of the Chief Financial Officer (OCFO), Office of Institutional Assurance (OIA), and Internal Audit Services (IAS). The project team was assigned responsibility for implementing OMB Circular A-123. Internal Audit's role was limited specifically to testing items that management deemed high risk. DOE Chicago provided guidance and oversight for the implementation process. DOE Berkeley Site Office provided oversight of the overall process and took extra steps to ensure the adequacy of the OMB A-123 implementation by assisting in testing.

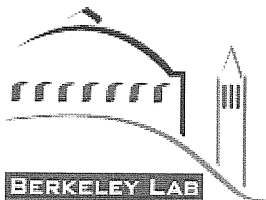
The OCFO's assessment and IAS' test work were reported in a template provided by DOE Chicago. The completed Site A123 Assessment and Reporting Tool (Site AART) was submitted to DOE Chicago on September 6, 2006.

Purpose and Scope

The purpose of this report is to communicate our observations for opportunities for improvement that were identified as a result of our testing efforts. Year two provides an opportunity to leverage what has been learned and to strengthen the link between internal control and financial reporting.

Year one implementation began in December 2005 and was completed in September 2006. We followed guidance provided by the Department of Energy *Office of the Chief Financial Officer* and implemented OMB Circular A-123 in three phases:

- Phase I - Documentation of key business processes under the direction of the OCFO completed February 17, 2006.
- Phase II – Evaluation of key business processes including identification of risks and controls and risk assessment under the direction of the OCFO completed March 15, 2006.
- Phase III – Testing under the direction of Internal Audit completed August 31, 2006. The scope of Internal Audit's work was limited specifically to testing items that management



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deemed high risk. The testing scope included transactions occurring from October 1, 2005 through July 31, 2006.

Conclusion

Approximately 350 controls were identified and tested with an overall Pass rating. Rating was limited to Pass or Fail. All DOE milestones were met on time and LBNL was praised by DOE Chicago for a job well done. The first year implementation was performed using only internal resources, which limited costs. Year two implementation activities should prove to be less time-consuming due to a number of factors, including:

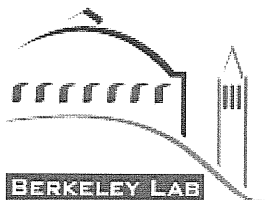
- Documentation of key business processes and internal controls was completed in year one. This was a time-consuming undertaking that will not be repeated in year two. Only newly identified or revised controls will need to be documented.
- Remediation work required for 2006 was completed.

Lessons Learned

Although the first-year implementation was challenging, most participants agreed that there were some benefits gained from the process. Most notable is the comprehensive identification of internal controls and testing that helped establish a foundation for the future. In addition, the improved knowledge of business processes and motivation to integrate principles of good governance and internal control into decision-making and day-to-day activities should facilitate sustained compliance.

While results of the implementation were good, there were opportunities for further improvement. To that end we make the following observations:

1. Management should prompt DOE Headquarters for clear and timely guidance. Planning for year two should begin as soon as possible in order to identify critical deadlines and resources required to meet those deadlines. In year two the focus will shift from the identification and documentation of key controls to more of a focus on testing. Management may want to evaluate the skill sets required to carryout the project objectives. If required skill sets are not available within the existing project team, training will need to be developed in testing and documentation of test work.
2. Continued senior management support will ensure an appropriate "tone at the top." Meetings with the OMB A-123 steering committee, comprised of senior management, are scheduled monthly. Pertinent information from documented steering committee meeting minutes should be shared with line management to demonstrate senior management support and to clarify project direction.



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3. Management should clearly define roles and responsibilities. Process owners must understand their role as control owner and be held accountable for identifying and updating key controls in their areas of responsibility. Project Team roles and responsibilities will need to be redefined as project objectives have shifted from documentation and evaluation to refining existing work and testing.
4. OMB A-123 is not a one time project. Therefore, control documents should be consistently updated when new, revised or previously unidentified controls are discovered. Management should ensure that control documentation is kept current.
5. A webpage may prove to be a more effective method for managing the large quantity of project related data that currently resides on a shared file. The shared file has become cumbersome with the vast quantity of data. Management should consider the cost benefit of developing an OMB Circular A-123 webpage with easy access links to guidance summaries and FAQ's for each step of the process.
6. Each division is encouraged to establish a method to charge and track all effort and costs associated with OMB A-123. This would provide the opportunity to evaluate whether costs associated with the OMB A-123 project are effectively managed. The OCFO will establish a project number for this purpose.
7. Change control - The OMB A-123 Team should evaluate an effective change control process to identify changes to control documentation. Once a best fit methodology is identified, it should be used consistently.